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**DETERMINANTS OF CAPITAL STRUCTURE: EVIDENCE FROM
MALAYSIAN SMEs**

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MASTER OF SCIENCE (INTERNATIONAL ACCOUNTING)

UNIVERSITI UTARA MALAYSIA

June 2017

**DETERMINANTS OF CAPITAL STRUCTURE: EVIDENCE FROM
MALAYSIAN SMEs**

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UUM
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**Thesis Submitted to Othman Yeop Abdullah Graduate School of Business,
Universiti Utara Malaysia, In Fulfillment of the Requirement for the Degree of
Master of Science (International Accounting)**



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ABSTRACT

This paper aims to investigate the determinants of capital structure of small and medium enterprises (SMEs) from manufacturing sector in Malaysia. Specifically, this study wants to examine the effect of asset structure, profitability, quality of information, size and age on leverage. Multivariate regression analysis and Pearson's correlation analysis were used to investigate the most significant factors that affect the capital structure choice of Malaysian SMEs during the year 2013. In the first model, both results find a negative and significant relationship for profitability and size with leverage while asset structure, quality of information and age show negative but not significant relationship with leverage. However, using a second model, asset structure shows a significant positive relationship with leverage, while quality of information shows significant negative relationship with leverage. The analysis indicates that firstly; the results are consistent with some capital structure theories such as trade-off theory and pecking order theory. Secondly, quality of information, asset structure, profitability and size are important factors that affect capital structure choice of Malaysian SMEs.

Keywords: Capital Structure, leverage, SMEs, pecking order theory, trade-off theory

ABSTRAK

Kajian ini bertujuan untuk mengkaji faktor-faktor yang mempengaruhi struktur modal dalam industri kecil dan sederhana (IKS) dalam sektor pembuatan di Malaysia. Secara khususnya, kajian ini bertujuan untuk mengkaji kesan struktur aset, keberuntungan, kualiti maklumat, saiz dan usia ke atas leveraj. Analisis regresi bersilang dan analisis korelasi Pearson digunakan untuk mengkaji faktor-faktor yang paling memberi kesan ke atas penentuan pemilihan struktur modal oleh syarikat-syarikat IKS di Malaysia. Dalam model pertama, kedua-dua hasil ujian menunjukkan faktor keberuntungan dan saiz adalah berkait secara negatif dan signifikan dengan leveraj manakala struktur aset, kualiti maklumat dan usia adalah negatif dan tidak signifikan dengan leveraj. Walau bagaimanapun, dengan menggunakan model kedua, kualiti maklumat didapati berkait secara negatif dan signifikan dengan leveraj, manakala struktur aset pula adalah berkait secara positif dan signifikan dengan leveraj. Analisis kajian menunjukkan bahawa pertamanya; dapatan kajian ini adalah bersesuaian dengan teori struktur modal seperti '*trade-off theory*' dan '*pecking order theory*'. Kedua, kualiti maklumat, struktur aset, keberuntungan dan saiz adalah faktor-faktor penting dalam menentukan pilihan struktur modal oleh syarikat-syarikat IKS di Malaysia.

Kata kunci: Struktur modal, leveraj, IKS, '*pecking order theory*', '*trade-off theory*'

ACKNOWLEDGEMENT

In the name of Allah, the Beneficent and the Merciful. Power and authority belongs to Allah along, who can decide a future to be certain, and who gave me the opportunity to undertake this study and eventually make it possible.

I would like to start with special appreciation to my lecturers in the School of Accountancy, College of Business in the Graduate School of Business (OYA) as a whole, especially those who taught me in one course or the other. My profound gratitude goes to my amiable supervisor Prof. Dr. Azhar Bin Abdul Rahman for his valuable guidance, advices, patience, and generous amount of time and support in guiding me which made this research successful.

I wish to express my indebted gratitude and acknowledgement to my parent in person of Masor Bin Dolah and Sharifah Binti Lateh for their caring, loving, support and concern given to me throughout my life. My propound appreciation also goes to my brothers, sisters and the entire family members for their support and prayers.

Finally, my appreciation goes to all my colleagues especially in person of Mohammad Fazzarudin bin Mohd Sabri, Maimuna Yahaya Kansila, Siti Zulaikha Zolkepli, Mozian Abuzaid Abdalla, Nor Fazana Che Ya and all my friends those supported me either direct or indirectly in order to finish this thesis. You are always been there giving me moral support and sharing tears, laughter and happiness and have made my life in UUM a lot of memories.

May the blessing of Allah be upon us in the here and Here-after.

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LIST OF ABBREVIATIONS

AS	:	Asset Structure
CCM	:	Companies Commission of Malaysia
EBIT	:	Earnings Before Interest and Tax
FS	:	Financial Statement
GDP	:	growth domestic product
GLCs	:	Government-linked Companies
LEV	:	Leverage
MASB	:	Malaysian Accounting Standards Board
MFRS	:	Malaysian Financial Reporting Standards
MITI	:	Ministry of International Trade and Industry
MM	:	Modigliani and Miller
MNCs	:	Multinational Corporations
MOSTI	:	Ministry of Science, Technology and Innovation
MPERS	:	Malaysian Private Entities Reporting Standards
NSDC	:	National SME Development Council
OLS	:	Ordinary-Least-Squares
PERS	:	Private Entity Reporting Standards
POT	:	Pecking Order Theory
PROF	:	Profitability
QUAL	:	Quality of Information
RM / MYR	:	Ringgit Malaysia
ROA	:	Return on Asset
ROE	:	Return on Equity
SME	:	small and medium sized enterprises
SMIDEC	:	Small and Medium Development Corporation
TOT	:	Trade of Theory
VDP	:	Vendor Development Program

CHAPTER ONE

INTRODUCTION

1.0 Introduction

This chapter aims to present an overview of the importance of capital structure of SMEs and to briefly discuss the background of SMEs in Malaysia. This chapter also provides discussions on the background of the study, problem statement, research question, research objective, scope and limitations of the study, and lastly, the organisation of the thesis.

1.1 Background of the Study

Financing decision is one of the most significant decisions that a firm need to consider as this decision can influence the firm value and determine whether a firm can expand its business or face bankruptcy. A wrong decision made by the manager may lead to financial distress and ultimately affect the business activity. In this light, a blend of securities and financing sources by an organisation to finance its investment activities is known as capital structure (Zabri, 2012), and managers play a significant role in selecting the best financing source that matches the business organisation.

The financing sources available either through equity or debt. The equity is given by the proprietor and shareholders, while, debt is acquired or obtained from banks and

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